

## **IDAHO FORECAST DESCRIPTION**

### **The Forecast Period is the Third Quarter of 2005 through the Fourth Quarter of 2008**

The Gem State's economy once again outperformed the Division of Financial Management's (DFM) prognostications. There is a pattern emerging. One, DFM forecasts the outlook for the state's economy. Two, actual job and personal income growth is stronger than had been anticipated. Three, based on the new actual data, DFM raises its economic forecast. Four, a new round of actual data shows job and income growths are even higher than in the revised outlook. Five, return to step one. For example, the forecasted Idaho nonfarm employment growth rate for 2005 was raised to 2.5% in July 2005 from 1.9% in April 2005. However, recent data supplied by the Idaho Department of Commerce and Labor show July's forecast was too low. As a result, the nonfarm employment growth rate for this year has been raised to 3.6% in the current forecast. At this pace, Idaho should have an average of about 609,000 jobs in 2005, or roughly 7,000 more jobs than had been forecast in July 2005.

The pattern described above traditionally occurs when one attempts to predict the speed of a fast-growing economy. A look at nonfarm employment and income show Idaho's economy has been growing fast indeed. Nonfarm employment advanced at a remarkable 6.8% annual rate during this year's first quarter—its best showing since 1994's second quarter. This year's strong start was followed by a 2.4% nonfarm employment gain in the second quarter of 2005. These gains are being fueled by the construction sector. Idaho construction employment soared to 45,500 in the second quarter of 2005. In July 2005 it was predicted annualized Idaho housing starts would peak at just under 23,000 units in this year's first quarter then decline to 21,200 units in the following quarter. More recent data suggest Idaho housing starts' first quarter peak was higher than predicted in July 2005 and its second quarter decline was not as steep as had been forecasted. Specifically, there were 23,300 annual housing units started in the first quarter and 22,600 units in the second quarter.

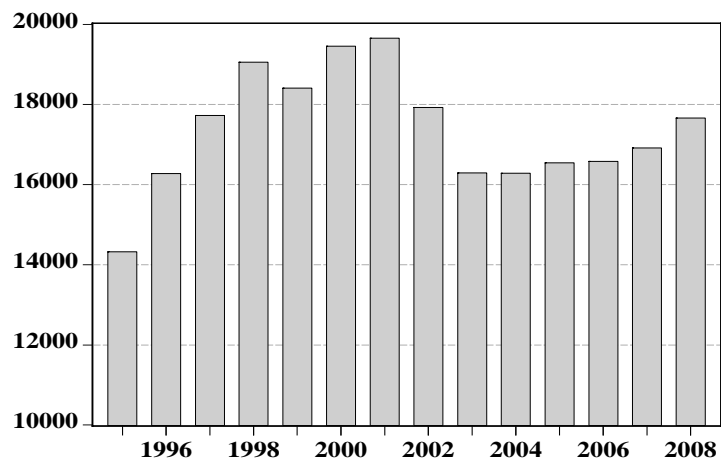
Idaho nominal personal income also improved in the first quarter of 2005, but this change is harder to detect because of a recent data revision. Specifically, a casual comparison shows Idaho personal income in the first and second quarter is actually lower in this forecast than in the July 2005 forecast. This is because the U.S. Bureau of Economic Analysis (BEA) revised its historical Idaho personal income estimates downwards back to 2002. Thus, the base has changed. In order to get an idea whether Idaho personal income was stronger than had been previously forecast, one needs to focus on the growth rates and not the levels of personal income. According to BEA's revised series, Idaho nominal personal income rose at an 8.6% annual rate in the first quarter of 2005 and by 6.7% in the second quarter. Under BEA's previous methodology, Idaho nominal personal income grew at a 4.3% annual pace in the first quarter of 2005 and DFM predicted it rose 2.8% in the following quarter. On an inflation-adjusted basis, the revised BEA data show Idaho personal income rose 6.2% and 3.4% in the first and second quarters of 2005, respectively.

Idaho's stronger-than-expected nonfarm and personal income performances in the first half of this year has once again raised the forecast's bar. Idaho nonfarm employment is projected to increase 3.6% in 2005, 1.8% in 2006, 2.0% in 2007, and 2.1% in 2008. Under these conditions, Idaho nonfarm employment will rise to about 646,700 jobs in 2008, which is about 9,000 jobs above the previous forecast. Idaho nominal personal income should grow an average of 6.5% over the forecast period, a noticeable improvement over July 2005's 5.9% average annual growth rate. Idaho real personal income is forecast to increase an average of 4.2% per year.

## SELECTED IDAHO ECONOMIC INDICATORS

**Computer and Electronics:** Idaho's large computer and electronics manufacturing sector now finds itself in relatively safe waters after navigating tumultuous seas for a couple of years. To appreciate the significance of this sector's current stability, one must divide this sector's journey into three legs. The first period is the expansion. Computer and electronics was one of the state's fastest employment growing sectors from the late 1980s to the late 1990s. During this period several factors combined to create near perfect conditions for rapid growth. These factors included the growing sophistication of personal

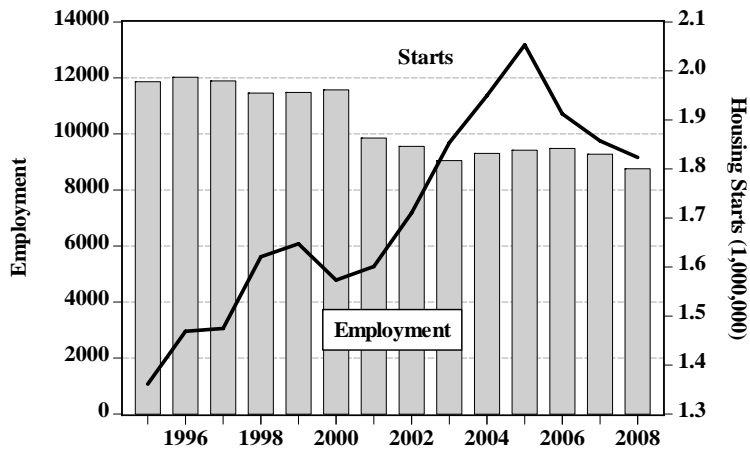
**Idaho Computer and Electronic Products Employment**



computer hardware and software that was a boon to local memory manufacturer Micron Technology. In addition, Micron's computer manufacturing subsidiary grew along with the popularity of personal computers. Hewlett-Packard's Boise plant prospered thanks to its phenomenally successful laser printer line. Zilog and AMI designed and produced application specific integrated circuits for a wide variety of products. Thanks to the success of these and other Idaho-based high-technology companies, Idaho computer and electronics employment advanced an average of 6.3% per year from 1991 to 2001. Near the beginning of the expansion, this computer and electronics sector overtook the logging and wood products sector to become the state's largest durable manufacturing employer. It next topped the food processing sector to become the state's largest manufacturing employer in 1997. Indeed, at least for awhile, this sector's growth seemed unstoppable. The computer and electronics manufacturing sector sailed into a squall in the first part of this decade. The casualty list from this turn of events included most of Idaho's biggest players. Jabil Circuit, a relatively new arrival on the Gem State's high-tech scene, halted a planned expansion and eventually closed its doors after customers' orders evaporated. In 2001, MicronPC.com, SCP Global Technologies, Micron MCMS, AMI, and Hewlett-Packard reduced their staffs. At first, this sector had enough momentum to weather the slowdown, though its employment growth slowed from 5.7% in 2000 to 1.0% in 2001. Unfortunately, the next year was not as prosperous. The Gem State's computer and electronics sector suffered another round of layoffs in 2002, this time employment did not just slow; it plunged 8.8%. One notable exception to the early rounds of layoffs was Micron Technology. However, the state's largest employer eventually succumbed to the high-tech downturn and reduced its Idaho workforce by about 1,000 in early 2003. The good news is the high-tech storm appears to be over, and the state's computer and electronics sector is entering a period of relative calm. This third leg of the voyage began in late 2003, as employment began to stabilize. Since then, Micron's payroll is back to its pre-layoff level. Businesses are again investing in equipment, and this should translate into high-tech jobs in the Gem State. However, employment is not anticipated to expand as rapidly as it had during the first leg of its journey. Specifically, Idaho computer and electronics manufacturing employment should advance 1.6% this year, 0.2% next year, 2.0% in 2007, and 4.4% in 2008. This forecast does carry a couple of downside risks. Hewlett-Packard recently announced it plans to reduce its company workforce by about 15,000 over the next 18 months. However, the company has not released details of the impacts this move will have on the Boise site. Because of this lack of data, no impacts from the company's latest

round of restructuring have been built into this forecast. Another challenge this sector faces is the potential glut of supply in the global semiconductor market.

### Idaho Wood Product Employment and U.S. Housing Starts



**Logging and Wood Products:** It appears that the state's logging and wood products sector has longer legs than had been previously forecast. It was reported in the July 2005 *Idaho Economic Forecast* that logging and wood products employment would decline from about 9,300 in 2004 to 8,600 in 2008. It is now believed Idaho logging and woods product employment will be relatively stable this year and next, then fall gradually to about 8,800 in 2008. There are two main reasons for this revision. First, actual Idaho lumber and wood products employment has been stronger than had been forecast. The most recent

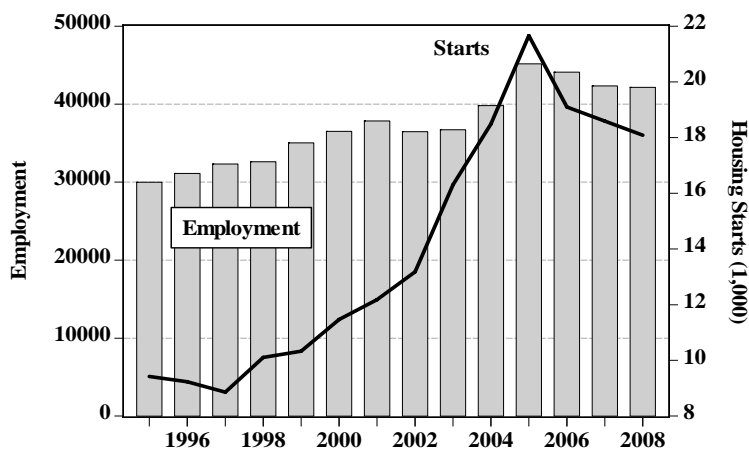
data from the Idaho Department of Commerce and Labor show logging and wood products employment advanced at a 9.9% annual rate in the first quarter of 2005 and declined just 0.5% in the second quarter of 2005. As a result, mid-year employment was just under 9,500, which is higher than the previous forecast of 9,200. Second, Idaho logging and wood products employment forecast was raised to reflect the anticipated stronger demand for building materials. Evidence for this can be found in the forecasted higher output for wood products. Specifically, the index for wood products production (1997= 100.0) is projected to be 102.2 in 2005, 106.9 in 2006, 104.8 in 2007, and 98.0 in 2008. In comparison, this same measure was anticipated to be 102.0 in 2005, 98.8 in 2006, 95.2 in 2007, and 94.8 in 2008 in the July 2005 forecast. This sector is also being helped by the weaker U.S. dollar, which is making U.S. wood products more competitive compared to Canadian products. Although the demand for logging and wood products has improved, Idaho employment gains will be limited by local capacity constraints and ongoing efficiency measures. Idaho manufacturing capacity is limited because several mills have been closed in recent years and the surviving mills have been forced to produce more products with less labor in order to remain viable. It has been estimated each Idaho logging and wood products employee produced about 215,000 board feet of lumber in 2003, which is well above the 172,000 board feet of lumber per worker produced in 1993. Idaho logging and wood products employment is expected to be 9,420 in 2005, 9,481 in 2006, 9,277 in 2007, and 8,758 in 2008. Idaho's logging and wood products sector should bask in relative stability over the next couple of years, but there are clouds of uncertainty on the horizon. The biggest concern is timber supply. The Gem State's logging and wood products sector has been traditionally dependent on timber from public lands, but this source has been shrinking over time. According to the U.S. Forest Service, just over half the timber harvested in Idaho came from public lands in 1993. By 2003, public timber accounted for less than 30% of the total harvest. A significant part of this decline is due to reduced harvests from national forests. The U.S. Forest Service estimates the harvest from Idaho national forests fell from 586.2 million board feet in 1993 to 123.2 million board feet in 2003, a decline of nearly 80%. Looked at another way, in 1993 timber from national forests accounted for more than a third of the total harvest, but just over 12% in 2003. Another concern is the current manufacturing over capacity. Strong markets in the 1990s led to heavy capital investment in this sector. As a result, it is estimated the industry can produce 20% to 25% more lumber than is being consumed in North America. This capacity is not currently a problem because of strong demand, but can lead to softer prices when demand ebbs.

**Mining:** Idaho's mining sector is enjoying a rare period of stability that should continue through next year. After shedding over 40% of its jobs from 1997 to 2002, Idaho's mining sector eked out a 16-job increase in 2003. Since 2003, this sector has continuously progressed. For example, in 2004 its employment advanced 8.2%, which was its strongest year-over-year gain since 1996. Mining employment is forecast to top 2,000 this year for the first time since 2000. And if the forecast holds, mining will have grown in four consecutive years. The last time this happened was in the mid-1990s. However, Idaho mining employment is not expected to approach its previous peak of nearly 3,000 jobs that occurred in 1997. This trend is consistent with this sector's recent history. A timeline of Idaho mining employment displays a downward trend in which any given peak in employment is smaller than the preceding peak. The current situation is no exception. For example, Idaho mining employment's previous apex was 3,000 in 1997, but its next peak in 2006 is projected to be about 900 jobs lower. While the mining industry has found fair haven, the ebb tide of declines will eventually reduce employment in the out years of the forecast. Specifically, Idaho mining employment is forecast to peak near 2,100 jobs in 2006, but drop to about 1,500 jobs in 2008.

**Construction:** Construction is both a trump card and wild card in the current *Idaho Economic Forecast*. First, the trump card. Much of Idaho's recent economic strength is tied to the state's strong housing industry. Quarterly data show Idaho housing starts jumped from around 16,500 annual housing starts in the first quarter of 2004 to a peak of nearly 23,300 units in the first quarter of 2005, a 41% increase. Housing starts have fallen to just under 22,600 units in the second quarter of this year, but this is still high compared to historical levels. The housing sector's recent strong performance was fueled by low mortgage

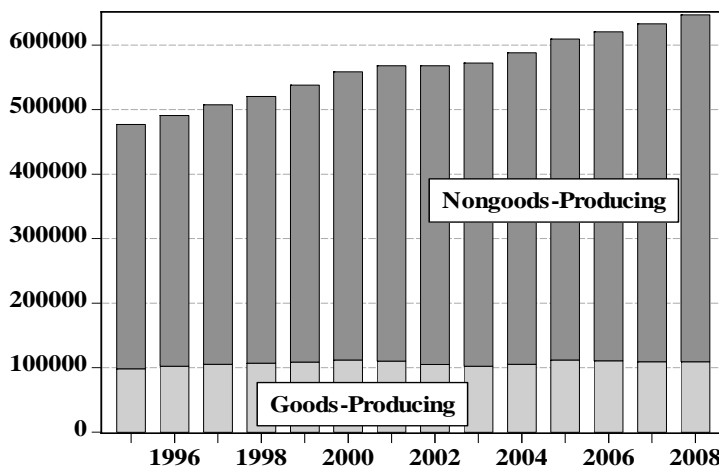
interest rates, strong personal income growth, and healthy population growth. It should be pointed out that actual housing starts are much stronger than had been predicted last summer. For example, in July 2005 it was reported annualized Idaho housing starts would peak at 20,775 units in the first quarter of this year. In the current forecast, housing starts peak at 23,284 units in the first quarter of 2005, an increase of about 500 units over the previous forecast. Likewise, Idaho construction employment has also grown much faster than had been anticipated. Specifically, in July 2005 it was predicted Idaho construction employment would rise at an 11.9% annual rate in the first quarter of 2005 and by 6.7% in the following quarter. Idaho construction employment actually advanced at a 29.1% annual rate in 2005's first quarter and 16.5% rate in the second quarter of 2005. As a result, Idaho construction employment stood at 45,500 at mid-year, which was substantially above the previous estimate of 42,900. There is no question the housing industry has been a major contributor to the state's current economic success. But there remains the question of its role in shaping the future. Mortgage interest rates and population growth have helped propel the state's recent housing boom. Mortgage interest rates have begun to rise from their record lows and are expected to continue rising over the forecast period. Idaho's population growth, which was nearly 2% in 2004, should taper down to 1.5% in 2008. These factors suggest Idaho housing starts and construction employment are near their respective peaks. The wild card is how fast and how steeply housing starts and construction jobs will decline.

**Idaho Construction Employment and Housing Starts**



There are several reasons why the state's housing boom will not turn into a bust. First, interest rates and population growth are expected to change gradually, giving the industry ample time to adjust. Second, although the Idaho housing sector has been robust, there does not appear to be a serious excess inventory of properties in the state. Third, recent studies to identify communities vulnerable to "housing bubbles" show no Idaho communities are at significant risk (most "bubbles" are concentrated on the coasts). Fourth, Idaho could benefit from a boom in second homes. In light of these factors, Idaho's housing sector is not expected to suffer an abrupt reversal of fortune. Instead, both Idaho housing starts and construction employment should decline gradually from their respective record levels over the forecast period. Specifically, Idaho housing starts should go from 21,700 units in this year to 18,100 units in 2008. Idaho construction employment is projected to decline from 45,200 to 42,200 over this same period.

### Idaho Nonfarm Employment



**Nongoods-Producing Industries:** The nongoods-producing sector's importance to Idaho's economy is measured in both its size and strength. For purposes of this section, the focus will be on the private, or nongovernmental, portion of nongoods-producing employment. Idaho government employment is covered in the following section. First, in 2004, the private portion of nongoods-producing employment accounted for over six of every ten nonfarm jobs. Second, Idaho nongoods-producing employment grew an average of 3.8% from 1991 to 2004, which was significantly faster than total nonfarm employment's 3.1% annual

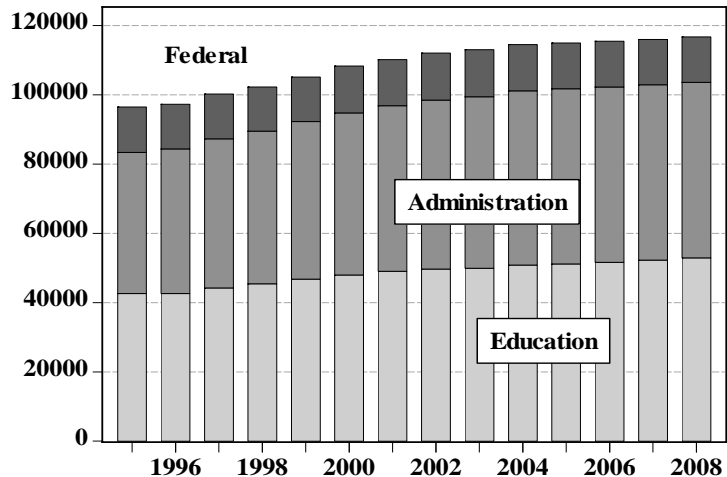
average pace. Nongoods-producing employment is split into two major categories: services and trade. The services category is the larger of the two, accounting for about 70% of the jobs. Services have also been the fastest growing of the two categories from 1991 to 2004. Specifically, services employment advanced an average of 5.0% per year while trade employment grew 2.4% annually. The services category consists of information services; financial activities, transportation, warehousing, and utilities; professional and business services; education and health services; leisure and hospitality services; and other services. The strongest performing components have been professional and business services and education and health services. The former component added jobs at a 6.4% average annual pace from 1991 to 2004 and the latter component's employment grew an average of 5.6%. The leisure and hospitality sectors and the other services sector both grew over 3% per year from 1991 to 2004. Over this same period, information services and transportation and utilities both increased 2.7% per year. Financial services advanced an average of 2.2%. Trade is the other private nongoods-producing sector category and is made up of wholesale and retail trade employment. Retail trade employment expanded at a 2.8% annual pace from 1991 to 2004 and wholesale trade employment increased at a 1.8% annual rate. Over the forecast period, Idaho total private nongoods-producing employment is expected to average 3.4% growth per year. Services employment should expand at a 3.5% annual rate and trade employment should increase an average of 3.2% per year.

**Government:** The general outlook for government jobs remains little changed compared to the previous forecast. Namely, the forecast calls for slow job growth for Idaho state and local governments over the next few years thanks to the state's cooling population growth. During the forecast period,

education-related employment should advance faster than noneducation-related employment. The difference largely reflects the need for local school districts to house their burgeoning student bodies. For example, the influx of students into the fast growing Meridian Joint School District, which includes West Boise, finds many of its new schools above capacity when they first open their doors. In response, school district patrons passed a bond to fund further the district's building needs. Interestingly, Meridian's eastern neighbor, the Boise School District, has actually seen its enrollment decline. However, plans to consolidate Boise

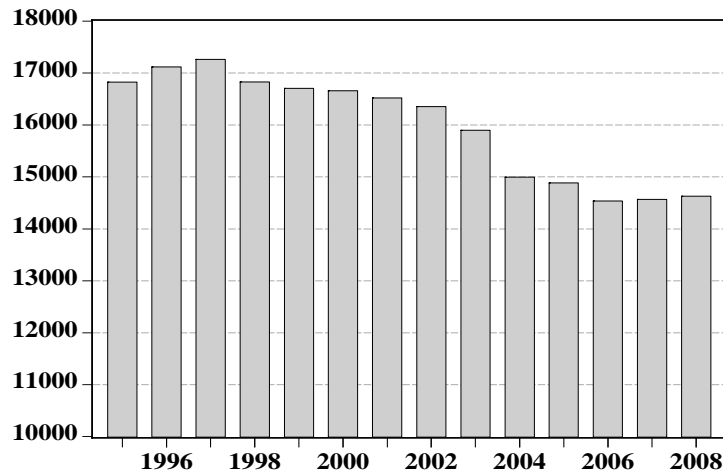
School District resources by closing some of its schools were shelved due to severe public resistance. The relationship between government employment and population is well established. Idaho's population grew about twice as fast as the nation's from 1990 to 2000, causing it to expand nearly 30% over the decade. Traditionally, Idaho's largest population gains are the result of migration. In fact, Idaho net migration was higher than the natural population (births less deaths) increase in every year from 1991 to 2000. The main reason the Gem State proved to be so attractive to newcomers is because in the 1990s it was viewed as an economic oasis in an economic desert. The Gem State proved especially enticing to Californians whose state was suffering its worst downturn since the Great Depression. Newcomers pouring into Idaho stretched the state's infrastructure. In an attempt to meet the fast growing population's demands for public services, Idaho's state and local employment payrolls expanded an average of 3.0% per year from 1991 to 2000. Migration slowed as other states prospered in the second half of the 1990s. By 2001, Idaho's natural population growth was actually above the migration increase. Idaho's population pace should taper off over the forecast period, dropping from 1.7% in 2005, to 1.6% in 2006, and to 1.5% in both 2007 and 2008. As a result, Idaho state and local government employment is projected to increase 0.6% in 2005, 0.5% in 2006, 0.6% in 2007, and 0.7% in 2008. Over this period, Idaho education-related employment should advance 1% annually and noneducation-related employment should rise 0.2%. Federal government employment should decline over the next few years. This decline reflects Congress' reaction to swelling federal budget deficits. The latest round of base realignments and closures that has been approved by President Bush will affect federal government employment in Idaho. It has been estimated 660 jobs will be lost, with Mountain Home Air Force Base taking the biggest hit. Unfortunately, the impact to the City of Mountain Home will be relatively high because Mountain Home Air Force Base is the city's largest employer.

## Idaho Government Employment



**Food Processing:** The state's food processing sector continues to evolve. Some of the changes in recent years have been painful, with several plants closing after decades of operation. For example, nearly 360 jobs were lost when unfavorable business conditions caused the J.R. Simplot Company to close its Nampa meat packing plant in the fall of 2003. In addition, the J.R. Simplot Company recently shuttered its Heyburn potato processing plant. The plant was built in 1960 and had run continuously since that time. More recently, the Swift and Company beef processing plant fell victim to the embargo of Canadian beef imports into the U.S. Concerns over mad cow disease restrict imports to animals under 30 months old. The Nampa plant processed older animals and was not able to get enough animals to keep operations viable. About four hundred jobs were lost when the company permanently closed the plant. Although some plants have closed, new plants are opening. For example, Gossner Foods, Inc.

### Idaho Food Processing Employment



doubled from 208,000 cows in 1994 to 404,000 cows in 2003. Over this same period, milk production more than doubled from 3.8 billion gallons to 8.8 billion gallons because of the increased output per cow. The amount of milk sold to plants also more than doubled during this time. Milk cash receipts grew from a little under one-half billion dollars in 1994 to over one billion dollars in 2003.

has opened a new cheese manufacturing plant in Heyburn on land formerly occupied by the J.R. Simplot plant. This fall Marathon Cheese announced it would build a \$27-million plant in Mountain Home. Company officials estimate the cheese-packing plant will initially employ 250 workers, but employment should climb to twice that many jobs in five years. This would make the plant one of Elmore County's largest employers. The new Gossner and Marathon cheese plants are symbolic of the state's growing dairy industry. According to the USDA, the size of Idaho's dairy herd has nearly